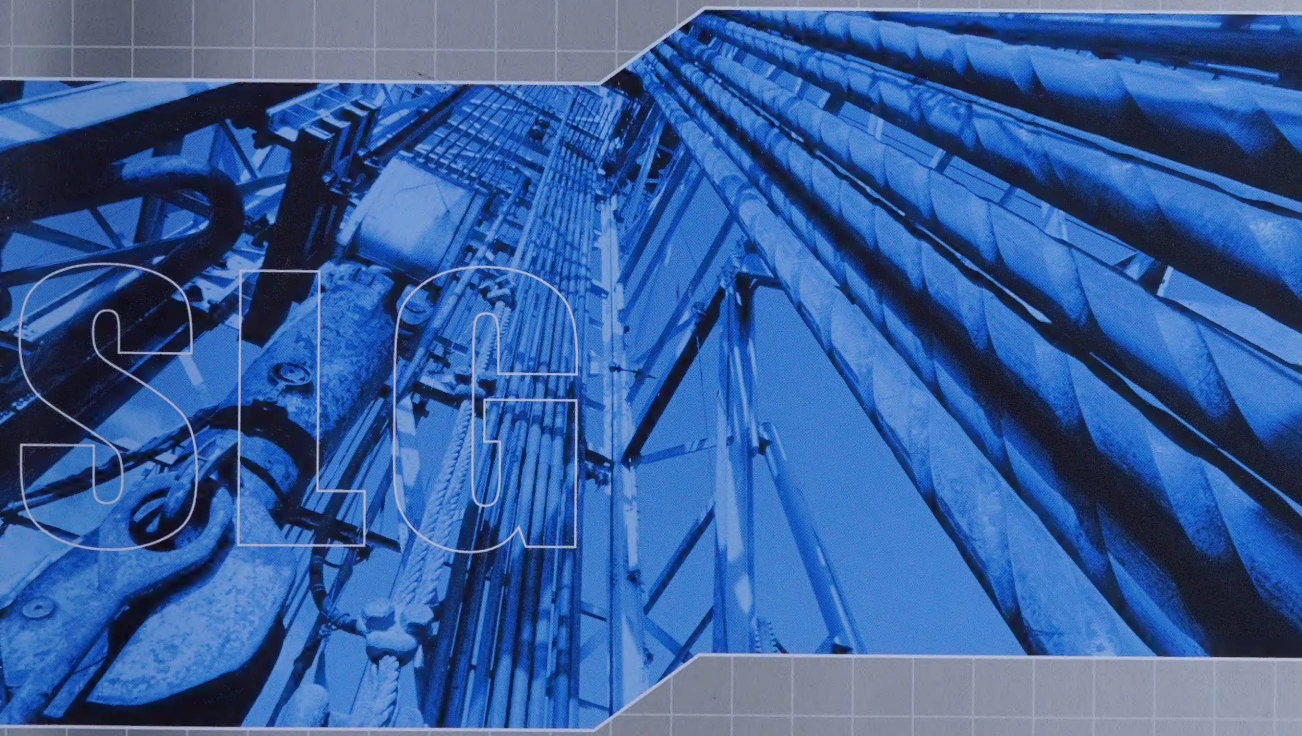
Sterling Resources Ltd.



Annual Report 2001

COMPANY PROFILE

Sterling Resources Ltd. is a Calgary, Canada based energy company actively engaged in the exploration and development of crude oil and natural gas in selected areas of the world. The Company's strategy for achieving growth is to source and initiate international projects with the potential for larger, lower-cost reserves. High initial working interests are taken where possible, and financial exposure and risk are managed by obtaining industry participations. Current landholdings are focused in the United Kingdom, Romania and Denmark. Sterling is actively seeking projects in certain countries in the Middle East and North Africa jointly with other petroleum companies. The common shares of Sterling Resources Ltd. trade on the Canadian Venture Exchange under the symbol SLG.

ANNUAL MEETING

An Annual General and Special Meeting of the Shareholders of Sterling Resources Ltd. will be held on Wednesday, May 29, 2002 at 10:00 a.m. (Calgary time) in the Cardium Room of the Calgary Petroleum Club, 319 Fifth Avenue S.W., Calgary, Alberta, Canada. Shareholders who are unable to attend the Meeting are requested to complete and return the Instrument of Proxy to Computershare Trust Company of Canada at their earliest convenience.

TABLE OF CONTENTS

Message to Shareholders

During 2001, Sterling focused on technical activities to bring several of its projects to a drillable stage, added new acreage to its core areas and drilled a follow up well to assess the Doina gas discovery offshore Romania. Drilling and pre-drilling activities in the UK were delayed for several months due to the foot and mouth epidemic, however during this period, technical work continued and plans for the year 2002 are to drill at least four key wells, each with the potential to increase the value of the company appreciably. In line with its strategy of managing financial exposure and technical risk by taking in industry partners, the Company is negotiating farm outs on several of its licences.

The pre-drilling activities for the West Compton-1 well on Licence PEDL 048 in the Wessex Basin were delayed due to the impact of the UK foot and mouth epidemic. Full planning approval was obtained in July 2001, the access road modifications and site preparation are underway, and the well is now expected to spud in the second quarter of 2002. The well will test a large structure to the west of the Wytch Farm oilfield. Sterling has farmed out half of its 45% interest in this well to another oil company. Given the proximity of the well site to existing infrastructure, production testing could be quickly initiated if the well results in a discovery.

Technical work on Sterling's other UK licences has resulted in the identification of several leads and potential drilling locations. In the Weald Basin, a well has been proposed by the operator to drill a structure on PEDL 070 in close proximity to the producing Stockbridge field. Planning has started and drilling is expected to commence in the third quarter. Technical studies over PEDL 068 in the Cleveland Basin of northeast England showed the potential to drill up dip of two older wells, which had tested gas. Planning activities for two potential drilling locations will be undertaken during the first half of 2002 with a view to drilling one of the wells in the fourth quarter. The area has established infrastructure for gas sales and prices are attractive.

In September the Doina 3 well offshore Romania was drilled to appraise the existing Doina discovery within the main sand section and evaluate an additional upper sand interval to the west of the original Doina well. The main Doina sand, which tested gas in the previous discovery well, was encountered close to prognosis, confirmed the extent of the gas-bearing main reservoir and had an overall net pay slightly better than expected. However, the shallower reservoir target was not well developed. The well was plugged and abandoned as a gas well. Studies are underway to determine options for development of the existing gas accumulation and include the potential for linking the Doina gas with other gas discoveries in the area. A reported oil and gas discovery just east of the northern Pelican Block of our offshore contract area has increased the prospectivity of Gasca, a very large seismically defined prospect mapped on the eastern boundary of the Pelican Block. Additional geological and geophysical work is being carried out on this part of the Pelican area.

Onshore Romania, a full data review of the eastern portion of the concession area was undertaken, old seismic was brought to digital status and reprocessed so that we now have a complete data base over that area. As a result of this work, two focus areas have been selected for further activity with a view to drilling at least one well in the latter part of 2002.

Sterling was awarded two new licences in Denmark at the beginning of the year. Licence 1/01 was chosen as it has potential for Zechstein reservoirs similar to those existing in the UK Cleveland Basin, and Licence 2/01

because of its potential for salt dome structures. Both licences are in the early stages of exploration. The geological and geophysical work carried out on Licence 5/97 indicated that the structures were smaller and deeper than originally believed, and accordingly, the partners decided to relinquish it.

Private equity financings were completed during 2001 for total proceeds of $3,355,580, the funds being used primarily for capital expenditures. During 2002, while gross capital expenditures will be higher due to the increased drilling, Sterling plans to cover a large portion through farm outs in accordance with its aforementioned strategy of managing financial exposure and technical risk by taking in industry partners.

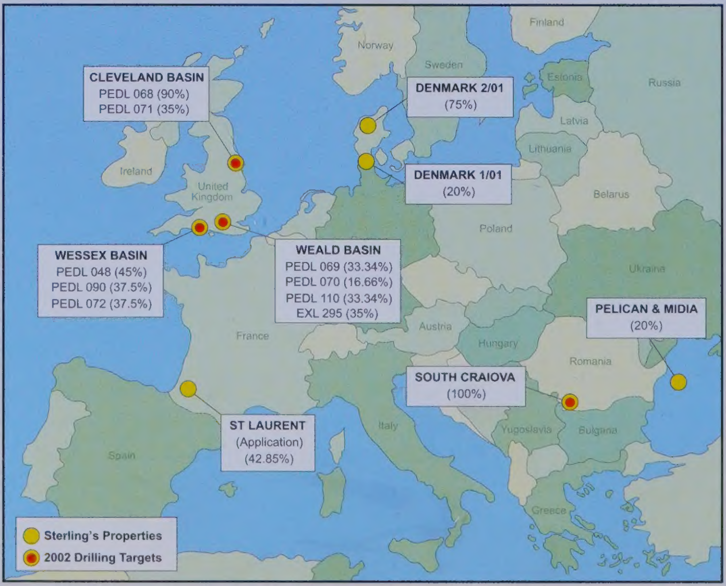
We wish to thank all our shareholders for their continuing interest and support. With our activities now moving more into the drilling phase, 2002 should be an exciting year for Sterling.

On behalf of the Board of Directors

Robert G. Welty
Chairman & Chief Executive Officer
March 8, 2002

Stewart G. Gibson
President & Chief Operating Officer

Sterling's Oil and Gas Properties



Operations Review

UNITED KINGDOM ONSHORE

Sterling currently has interests in 680,300 gross acres (306,950 net acres) and is operator for three of the nine onshore UK licences held.

The onshore UK continues as one of Sterling's main focus countries. Adding to its position established in the Wessex Basin in the 8th Round Licence application, the Company added significant interests in two other productive geological basins during the 9th Round Licence – the Weald and Cleveland Basins. During the 10th Round of applications, which closed in November 2001, a further one block application was made for a single block adjacent to Sterling's existing acreage in the Weald.

In addition to excellent fiscal terms, the onshore UK was selected for its good prospectivity. As well as being located within producing basins, several of Sterling's licences include discoveries. The licences are being evaluated with the benefit of more recent seismic, current drilling and completion practices and benefit from present day infrastructure and market conditions. Technical work completed during 2001 has enhanced the original concepts in several of the licences and, in addition to the well planned in the Wessex Basin, Sterling is currently pursuing planning for four additional well locations which will result in drilling in each of the three geological basins. In addition to the selected well locations, the technical work to date has identified further prospects and leads which will be matured during 2002.

The Wessex Basin

Sterling's three licences in the Wessex Basin have been reviewed both in a regional context and on a prospect basis utilising a significant seismic and well database. Since award, some 400 km of seismic data has been reprocessed and 50 km of new seismic acquired. The new results have allowed direct mapping of the Triassic Sherwood Sandstone, the main target, and resulted in a series of prospects and leads along the stable Wessex High. This high trends east to west and the Sterling licences are up dip from the Wytch Farm and Wareham fields, which are located on the eastern portion of the trend. Wytch Farm has recoverable reserves of approximately 450 million barrels from the Sherwood and overlying Bridport and Frome reservoirs.

The regional review included studies on the oil generating "kitchen" location and magnitude. Lying to the south of the Wessex High, the kitchen is calculated as having the capacity of generating sufficient hydrocarbon to fill Wytch Farm and all the mapped structures along the trend. The regional migration pathways have also been mapped and demonstrate the potential for sourcing Wytch Farm and the Sterling structures to the west from the southern kitchen prior to the period of major inversion which subsequently affected the area to the south of the stable Wessex High. A surface geochemical survey over the planned well location in PEDL 048 registered the presence of hydrocarbons.

The first well on this under-explored trend will be drilled on the West Compton prospect in PEDL 048. This is a fault closed structure with a Sherwood objective with significant reserve potential. The prospect is well defined with recent seismic and has the potential to be charged either from the south or by longer migration from the east. The West Compton well will evaluate one of twenty prospects and leads located within the Sterling licences. The major reserve potential is within the Sherwood, although several prospects are mapped

at Bridport level. The Bridport produces at Wytch Farm and Wareham and a well, Waddock Cross, drilled in 1982 on PL 090 encountered an oil column in the Bridport.

Originally planned to be drilled in 2001, the planning for the West Compton well was delayed significantly by the foot and mouth epidemic which prevented land access for planning related surveys. Full planning approval was given in July 2001 and the first civil works started in November. The completion of road access modifications is forecast for late March 2002 and the operator estimates the well will spud during the second quarter of 2002, with final timing linked to the date the drilling rig completes its current contract.

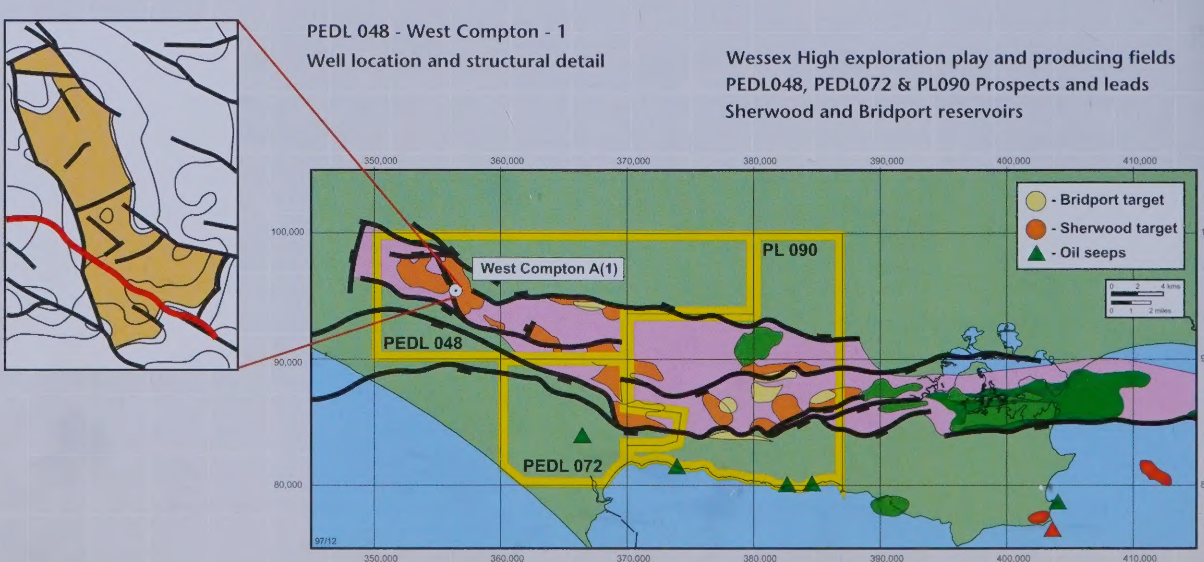
During 2001, work continued in refining drilling locations in PL 090 and PEDL 072. Activity on these blocks will be defined following results of the West Compton well.

The Weald Basin

Sterling's licences in the Weald Basin are located adjacent to the Stockbridge and Storrington fields, two of the eleven fields, which produce in the area. The main productive horizon is the Jurassic Great Oolite, a reservoir of variable quality with fracture production supplementing productivity. By applying recent drilling and completion practices, however, daily well rates have been significantly enhanced from production of a few hundred to in excess of 1,000 barrels per day. This, in conjunction with fracture identification techniques, has led to successful secondary recovery projects and related improvement in ultimate recovery.

During 2001, existing seismic and well data was acquired and evaluated within the portion of PEDL 069 which lies just to the west of the Stockbridge field. A number of closures have been mapped which are smaller than the

Wessex Basin



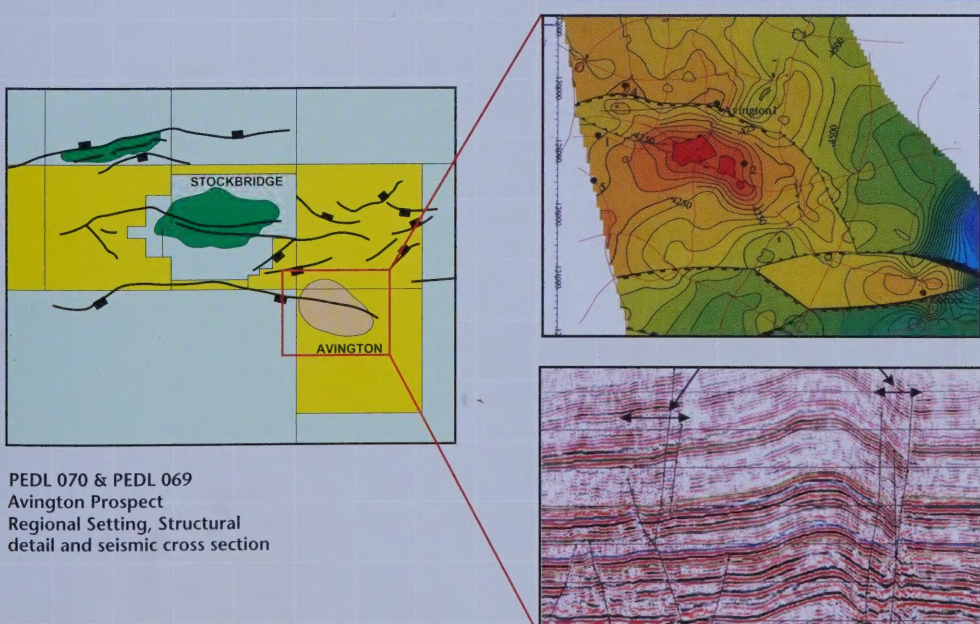
prospects in the eastern portion of the licence. These structures will be followed up after the 2002 drilling results on PEDL 070. The eastern part of PEDL 069 lies just to the east of the Stockbridge field and contains a mapped extension of the Avington prospect that is mapped in PEDL 070 which lies immediately south of PEDL 069.

PEDL 070 was acquired as a 9th Round Licence in partnership with Pentex, the operator of the Stockbridge field. During 2001, the group purchased existing seismic and completed an evaluation which included the Avington and Lomer wells, both of which contain oil columns. The recent work has firmed up the Avington structure which has the potential to contain large oil in-place volumes. The Avington well is mapped as having a 41 metre oil column (untested) in the footwall of a composite structure. Based on interpretation of the post well seismic coverage, significant hydrocarbon potential is now mapped in the hanging wall with a common hydrocarbon/water contact. As mentioned above, the northern part of the Avington structure is mapped as extending into PEDL 069.

As operator of PEDL 070, Pentex has proposed a well on the Avington structure for 2002. A location has been identified and planning discussions initiated.

Drilling plans for the Henfield – Oreham structure in Sterling's EXL 295 licence were also hampered by the foot and mouth epidemic. A licence extension has been granted to January 2003 by the UK Department of Trade and Industry to reflect this. Planning for the well location is now progressing. The operator has proposed a well up dip from the Henfield well which was drilled in 1938 and tested some gas from open hole tests. The

Weald Basin – PEDL 069 & PEDL 070



PEDL 070 & PEDL 069
Avington Prospect
Regional Setting, Structural detail and seismic cross section

well is targeting gas from the Great Oolite reservoir which produces from the Storrington field, adjacent to and down dip to the west of the location.

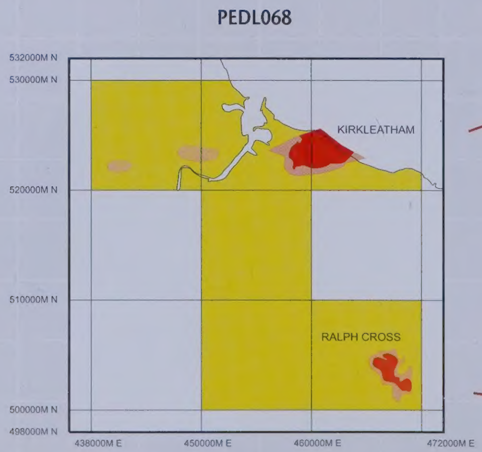
The Cleveland Basin

Activity during 2001 on PEDL 068 and PEDL 071 has focused on acquiring all relevant well and seismic data and refining the prospect definition that was available at the time of application. This work has been completed over the two main prospects in PEDL 068 and continues over the remainder of this licence and PEDL 071. Results to date are encouraging.

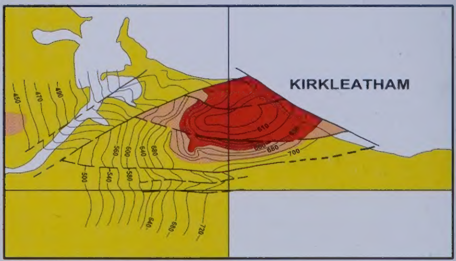
The area is gas prone and has five fields currently producing. The target reservoirs are the Permian Zechstein Carbonates and Rotliegendes Sandstone together with the underlying Carboniferous section. These reservoirs produce in the southern gas basin offshore the UK and the Netherlands. The area has an established infrastructure and direct gas sales are complemented in some areas by sales for conversion to electricity and for gas storage. This provides alternatives for maximizing prices

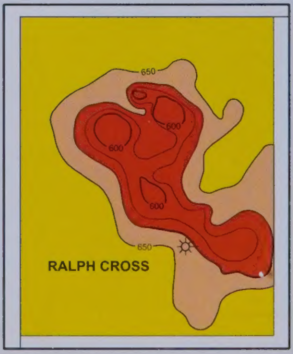
Three older exploration wells all encountered gas on PEDL 068 in the Zechstein Carbonates and a number of wells drilled for water or salt in the late 1800's also reported the occurrence of oil and gas. The first exploration wells were drilled by D'Arcy in the 1940's at Kirkleatham and tested gas from open hole tests, without the benefit of stimulation. The more recent exploration well drilled by Home Oil in 1966 at Ralph Cross tested gas at commercial rates, in excess of 3 mmcfd.

PEDL 068 – Kirkleatham & Ralph Cross Prospects



PEDL068 Kirkleatham and Ralph Cross prospects
Zechstein carbonate reservoir
Up-dip potential from tested gas





Review of seismic data which was collected after the discoveries at Kirkleatham and Ralph Cross shows the potential to drill up-dip of the older wells and target gas volumes which are potentially significant at both the Kirkleatham and Ralph Cross prospects. Given the nature of the reservoirs, horizontal well and modern well completion techniques will be adopted to maximise wellbore productivity and access to fracture zones.

Sub-surface locations have been selected for both the Kirkleatham and Ralph Cross prospects and planning discussions will be pursued for both in early 2002. The present outlook is for one of the wells to be drilled in 2002 and the second in 2003. Additional prospective structures are recognised in both the Permian and Carboniferous within PEDL 068 and these will be further refined and evaluated during the coming year.

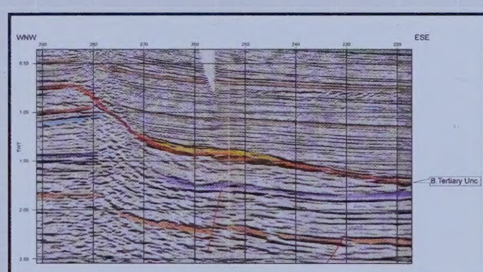
During 2001, activity on PEDL 071 focused on the eastern part of the block, close to the Caythorpe gas field. Data purchase and evaluation has identified a number of structural leads. It is planned to extend the data purchase and review during 2002.

ROMANIA ONSHORE

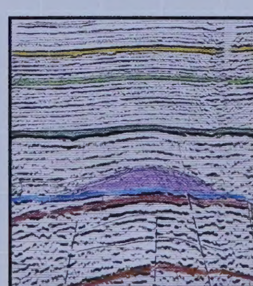
Sterling has a 100% working interest and operates the South Craiova Block under a Concession Agreement. This 1,545,000-acre block is located to the south and west of Bucharest and is part of the Moesian Platform, with its associated producing fields in Romania, to the north and east, and Bulgaria to the south. The South Craiova Block represents a large tract of prime exploration acreage which has been virtually unexplored with the aid and benefit of modern exploration techniques. The area has potential in several play types, all of

Onshore Romania

Base Tertiary unconformity play
Edge of Bailesti Depression
(Bradesti analogue)



South Craiova Licence
current areas of focus



East - West Reefal trend
(Bulgarian field analogue)

which produce in neighboring areas. The contractual terms are attractive and the ability to move rapidly to drilling exists, eased by the readily accessible terrain.

A large volume of historical data exists but much of this relates to shallow drilling and vintage analogue-type seismic. Portions of the block have 1970, 1980 and limited 1990 seismic coverage. During 2001, some 300 km of seismic was reprocessed. In addition, a full data review of the eastern half of the block was completed bringing all old data to digital status, including the analogue seismic data. The final product including the reprocessed seismic, was a complete database to provide mapping of the key structural elements.

As a result of the work to date, two focus areas have been selected for further activity. The first of these, in the northern part of the block, is concentrating on the base Tertiary unconformity as it rises to structural highs on both sides of the Bailesti Depression. The play is analogous to the Bradesti oilfield (100 mmbbls) which lies just to the north and east of the concession. Additional targets in this area are the Tertiary sands within the depression as well as sand infills in the Jurassic and deeper Triassic sands and Carbonates.

The second focus area lies just to the north of the Danube (the southern boundary of the concession) and is concentrating on a potential series of Malm-Neocomian reefal structures. These structures lie east-west on trend with the Gigen field in Bulgaria which produces from a reef development. In addition there is the potential for Triassic Carbonate traps, mapped with current data, which also produce in Bulgaria.

A surface geochemical survey is planned for both focus areas with results expected by mid 2002. The presence of anomalies will be used to define the next stage of activity, which will either include infill seismic or preparations to drill.

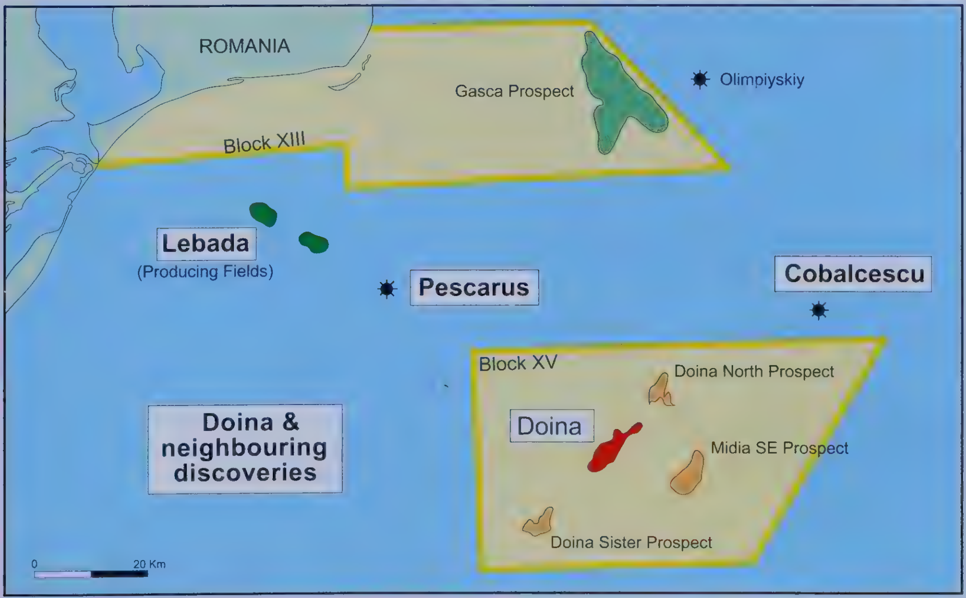
ROMANIA OFFSHORE

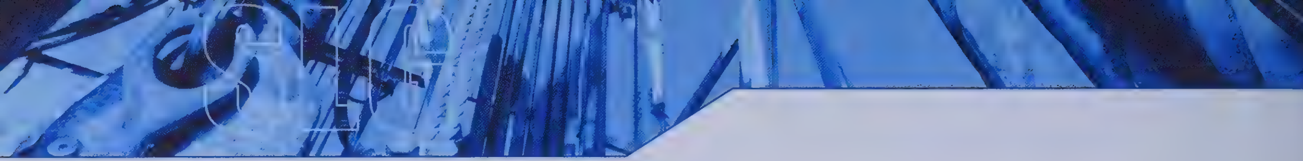
Sterling holds a 20% working interest in two blocks covering approximately 1.1 million acres offshore Romania. In the southern Midia Block XV an appraisal well Doina 3 was drilled in September 2001. Well operations using the Petrom owned Jupiter rig progressed to schedule and the well was completed within budget. The first objective of the well, to appraise the extent of the main Doina reservoir previously tested in the Doina 2 well, was successful. The gas water contact and the main sand body were encountered close to prognosis. The net to gross and quality of the main reservoir sand was better than expected.

The secondary exploration objective of Doina 3 failed to find a potential significant gas-bearing shallower section, which had been inferred from seismic. Since the upper unit was not developed and the main reservoir had been adequately tested in the Doina 2 well, Doina 3 was abandoned as a gas well. The additional prospectivity along the Doina trend remains and in particular, Doina Sister is still a viable drilling target.

Prior to further drilling on the block, the joint venture has elected to complete a study to determine options available for development of the existing gas accumulation. Consideration will also be given to scenarios linking the Doina area to nearby and potential discoveries for future development. The study should be completed by midyear 2002 and forward plans finalised in the second half of 2002.

On the northern Pelican Block XIII, the seismic program shot in 2000 included new lines across the eastern portion of the block. Evaluation of this new seismic, in conjunction with the database previously available, increased the prospectivity of Gasca, a very large prospect mapped on the eastern boundary of the block. Source and migration studies, completed in parallel, demonstrated the potential for filling the Gasca structure from the southeast, but this remained a large component of the overall prospect risk. However, towards the end of 2001, a well was drilled just to the east of the Pelican area (Olimpiyskiy) and this has reportedly tested oil and gas from at least two horizons and is to be further appraised. Based on the possible significant impact of these well results on the prospectivity of the Pelican Block, the group have taken a Prospecting Licence over the North Pelican area. This increased position will allow completion of a detailed regional study to include incorporation of the Olimpiyskiy well impact. The study will also be completed by mid 2002 and will allow the integration of forward planning for both the Pelican and Midia Blocks.





DENMARK ONSHORE

Sterling acquired a 75% operating interest in Licence 2/01 in March 2001. The licence, known as the Salling Block is located in North Jutland. The area has existing seismic and limited well data but has seen little activity since the early 1980's. Since award, Sterling has completed a geological review of the area to incorporate structural, reservoir and source details on both a regional and block specific basis. Based on this review, a portion of the existing seismic data was selected for reprocessing and this is currently ongoing.

The area is dominated by salt features which create significant structuring. The trapping potential on the flanks of the salt features is further enhanced by faulting and pinch outs, especially moving down dip towards the "kitchen" area. In terms of source, the Fjerritslev formation was found to have reached early maturity in two wells just to the east of the block. Studies indicate that full maturity is reached in the deep rim synclines which border the salt features. Some oil was recovered in an RFT sample from the Merjup well drilled just to the south of the Salling area. The main reservoir targets are the Triassic Gassum and the Jurassic Haldager formations.

Work to date has indicated two main areas of focus down flank to the north and east of the Skive salt feature. This evaluation will be refined following completion of the seismic reprocessing currently ongoing. In addition, a previous sparse surface geochemical survey indicated potential anomalies over the two focus areas. A new regular spaced survey is planned for 2002 and the results from all new data will be available by the third quarter of 2002.

Sterling also holds a 20% working interest in Licence 1/01 (South Jutland) which was also awarded in March 2001. This large 900,000-acre area lies on the Zechstein trend which produces in Poland and the eastern part of Germany.

The major part of the South Jutland area has not been explored for the last 10 to 20 years, and has therefore not had the benefit of modern exploration techniques. The group are currently reprocessing the majority of the existing 1,500 km seismic database and plan to conduct a surface geochemical survey.

A previous discovery, the Logumkloster well drilled in 1980, exists on the block. The well tested up to 15 mmcf/d of gas rich in nitrogen and up to 150 BOPD condensate from Zechstein carbonates. A number of wells within the licence encountered significant shows of hydrocarbons in the Zechstein.

The play concept for the area includes Zechstein "barrier edge" and "slope" plays analogous to multiple existing on-trend discoveries and production. A number of identified leads will be subject to further evaluation using the reprocessed seismic and geochemical data.

The geological and geophysical work carried out on License 5/97 indicated that the structures were smaller and deeper than originally believed, and accordingly, the partners decided to relinquish it.

FRANCE ONSHORE

Following a study of the unlicenced areas of France, Sterling was part of an application for a licence in the Adour-Arzacq sub-basin of the prolific Aquitaine Basin of southern France. The application was open for a period of competition, which closed in October 2001. Formal award is expected during the first half of 2002, following a period of review by the relevant regional authorities and the DGEMP.

The Ardour-Arzacq Basin has 15 producing fields and discovered reserves estimated at 13 tcf of gas and 100 mmbbls of oil. The basin has thick clastics in the Tertiary, Triassic and Carboniferous and Carbonate reservoirs in the Jurassic and Cretaceous. The presence of good source rocks and multiple structural styles (some related to significant salt features) complete the basic requirements for attractive exploration.

The St. Laurent Licence (pending award) covers some 294,000 acres and is located 20 km northwest of the giant Lacq field. Sterling has a 42.85% working interest in the application. Although significant pre 1980's seismic exists, little modern exploration has been undertaken in the area. In addition to a heavy oil accumulation which forms part of the licence area, oil and gas was present in a 1960's deep well and there are surface oil seeps. In the initial period, the old data will be reprocessed and evaluated to evaluate Mesozoic plays associated with salt ridges. The heavy oil discovery will also be reviewed to determine potential productivity utilising modern recovery techniques.

In April 2001, the operator of the Larcis Antin Block, also located in the Aquitaine Basin, elected not to renew the exploration permit. Sterling opted not to continue by itself, given the large work commitment on the block.

HEALTH, SAFETY AND ENVIRONMENT

Sterling Resources is committed to operate safely in an environmentally sensitive manner and to safeguard the health and welfare of its employees, contractors, suppliers and the public, in every area of operation.

Management's Report

The accompanying consolidated financial statements and all information in the annual report are the responsibility of management. The consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles outlined in the notes to the consolidated financial statements. Other financial information appearing throughout the report is presented on a basis consistent with the consolidated financial statements.

Management maintains appropriate systems of internal controls. Policies and procedures are designed to give reasonable assurance that transactions are appropriately authorized, assets are safeguarded and financial records properly maintained to provide reliable information for the presentation of financial statements.

Ernst & Young LLP, an independent firm of Chartered Accountants, has been engaged, as approved by the shareholders, to examine the consolidated financial statements in accordance with Canadian generally accepted auditing standards and to provide an independent professional opinion.

The Audit Committee and the Board of Directors have reviewed the consolidated financial statements with management and with Ernst & Young LLP. The Board of Directors has approved the consolidated financial statements on the recommendation of the Audit Committee.

R G Welty — Sherry L. Cremer

Robert G. Welty
Chairman & Chief Executive Officer

Sherry L. Cremer
Treasure & Corporate Secretary

Auditors' Report

To the Shareholders of Sterling Resources Ltd.

We have audited the consolidated balance sheets of Sterling Resources Ltd. as at December 31, 2001 and 2000 and the consolidated statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2001 and 2000 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Calgary, Canada
February 21, 2002

Ernst & Young LLP
Chartered Accountants

Consolidated Balance Sheets

As at December 31

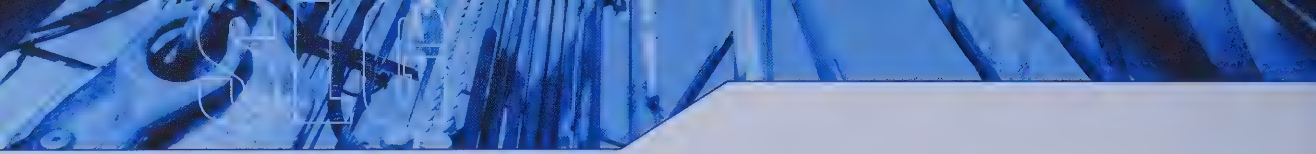
	2001	2000
	$	$
ASSETS		
Current		
Cash and short term investments *[note 4]*	634,552	98,231
Accounts receivable	89,151	95,500
Due from officers *[note 5]*	125,000	—
	848,703	193,731
Due from officers *[note 5]*	115,000	440,000
Capital assets *[note 6]*		
Petroleum and natural gas properties and equipment	7,557,514	5,208,977
Furniture and fixtures	29,033	33,280
	7,586,547	5,242,257
	8,550,250	5,875,988
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities	270,692	259,970
Commitments *[note 9]*		
Shareholders' equity		
Share capital *[note 8]*	11,612,046	8,310,328
Contributed surplus	66,479	66,479
Deficit	(3,398,967)	(2,760,789)
	8,279,558	5,616,018
	8,550,250	5,875,988

See accompanying notes

On behalf of the Board:

Director

Director



Consolidated Statements of Operations and Deficit

For the years ended December 31

	2001	2000
	$	$
EXPENSES		
General and administrative		
- corporate	562,208	706,713
- exploration projects	149,583	163,454
Depreciation	7,508	8,027
	719,299	878,194
OTHER INCOME		
Interest	81,121	28,525
Net loss for the year *[note 7]*	638,178	849,669
Deficit, beginning of year	2,760,789	1,911,120
Deficit, end of year	3,398,967	2,760,789
Net loss attributed per common share		
Basic	0.04	0.10
Diluted	0.04	0.10

See accompanying notes

Consolidated Statements of Cash Flows

For the years ended December 31

	2001 $	2000 $
OPERATING ACTIVITIES		
Net loss for year	(638,178)	(849,669)
Items not affecting cash		
Depreciation	7,508	8,027
Cash flow from operations	(630,670)	(841,642)
Change in non-cash working capital	17,071	124,312
Cash used in operating activities	(613,599)	(717,330)
INVESTING ACTIVITIES		
Petroleum and natural gas properties and equipment additions	(2,348,537)	(1,297,309)
Furniture and fixture additions	(3,261)	(2,165)
Cash used in investing activities	(2,351,798)	(1,299,474)
FINANCING ACTIVITIES		
Issue of common shares, net of share issue costs	3,301,718	502,600
Decrease in due from officers	200,000	100,000
Cash provided by financing activities	3,501,718	602,600
Increase (decrease) in cash	536,321	(1,414,204)
Cash and short term investments, beginning of year	98,231	1,512,435
Cash and short term investments, end of year	634,552	98,231

See accompanying notes

Notes to Consolidated Financial Statements

1. DESCRIPTION OF BUSINESS

Sterling Resources Ltd. (the "Company") is a publicly traded energy company engaged in the exploration, development and production of crude oil and natural gas in selected areas of the world.

2. SIGNIFICANT ACCOUNTING POLICIES

Consolidation and investments

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiary Sterling Resources (UK) Ltd. The consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. Because a precise determination of many assets and liabilities is dependent upon future events, the preparation of financial statements involves the use of estimates and approximations which have been made using careful judgment. The consolidated financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and within the framework of the significant accounting policies summarized below.

Petroleum and natural gas properties and equipment

The Company follows the full cost method of accounting for petroleum and natural gas operations whereby all costs relating to the acquisition of, exploration for and development of petroleum and natural gas properties and equipment are capitalized in cost centres on a country-by-country basis. Such costs include lease acquisition costs, geological and geophysical expenditures, lease rentals, and costs of drilling and equipping productive and nonproductive wells.

All cost centres are in the pre-development stage and as such the costs in each centre are not subject to depletion. The recovery of the costs incurred to date is uncertain and is ultimately dependent upon discovering commercial quantities of hydrocarbons. The likelihood of such a discovery is not determinable at this time.

Furniture and fixtures are carried at cost less accumulated depreciation. Depreciation is calculated on a declining balance basis at an annual rate of 30%.

Joint operations

Substantially all of the Company's exploration activities are conducted jointly with others and, accordingly, these financial statements reflect only the Company's proportionate interest in such activities.

Foreign currency translation

Operations in foreign countries are translated using the temporal method. Foreign currency denominated monetary assets and liabilities are translated at exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities denominated in foreign currencies are translated at rates in effect on the dates the assets were acquired or liabilities were assumed. Revenues and expenses are translated at rates of exchange prevailing on the transaction dates. Translation gains and losses are included in income.

Income taxes

The Company follows the liability method of accounting for income taxes. Under the liability method, the Company will record future income taxes for the effect of any differences between the accounting and income tax basis of an asset or liability. Future income taxes are measured using substantively enacted income tax rates.

Stock options

Under the Company's stock option plan, no compensation expense is recognized when stock options are issued to employees. Any consideration paid on exercise of stock options is credited to share capital.

3. CHANGES IN ACCOUNTING POLICIES

Earnings per share

The Company retroactively adopted the treasury stock method of computation, presentation and disclosure of diluted earnings per share as recommended by the CICA. Under the treasury stock method, only "in the money" dilutive stock options and other instruments impact the diluted calculations. The new method was applied retroactively with restatement of prior periods. The effect of the options outstanding using the treasury method would not be dilutive for the years ended December 31, 2001 and 2000.

Net loss per share is calculated based on net income as the numerator in the calculation and the weighted average number of shares issued and outstanding during the year ended December 31, 2001 of 14,289,979 (2000 – 8,676,256) as the denominator.

4. CASH AND SHORT TERM INVESTMENTS

Cash and short term investments include $415,000 (2000 – nil) of bankers' acceptances with maturities of less than 90 days, bearing interest between 1.57% and 1.66%.

5. RELATED PARTY TRANSACTIONS

During 1998, the Company loaned $225,000 to an officer of the Company for purposes of acquiring common shares in the Company. The loan is interest free and the principal sum is repayable in full on January 27, 2002. During 2000, the officer repaid $100,000.

During 1999, the Company loaned $315,000 to an officer of the Company for purposes of acquiring common shares in the Company. The loan is interest free and the principal sum is repayable in full on September 1, 2003. During 2001, the officer repaid $200,000.

Collateral for the notes consists of the common shares purchased. The Company has no recourse against the parties to the notes if the Company's share price subsequently declines.

During the year ended December 31, 2001, the Company paid $48,000 (2000 – nil) in consulting fees to a company controlled by one of the directors of the Company. These consulting fees have been recorded at their exchange amount and are in the normal course of operations.

6. CAPITAL ASSETS

(a) Petroleum and natural gas properties and equipment

	2001 $	2000 $
Romanian oil and gas properties	**4,686,801**	3,152,062
U.K. oil and gas properties	**2,600,900**	1,922,591
Other	**269,813**	134,324
	7,557,514	5,208,977

No general and administrative costs were capitalized in 2001 or 2000.

In order for the Company to maintain its working interests in its oil and gas properties in the pre-development stage, the Company has commitments to complete various seismic, geological, geophysical and other exploration work programs. The continuation of this work is dependent upon the ability of the Company to obtain continued financing and/or farm out any of its existing working interests.

(b) Furniture and fixtures

	2001 $	2000 $
Furniture and fixtures	**70,190**	66,920
Less accumulated depreciation	(41,157)	(33,640)
	29,033	33,280

7. INCOME TAXES

Income taxes differ from the amounts, which would be obtained by applying the statutory income tax rate to the loss before income taxes as follows:

	2001 $	2000 $
Computed income taxes (recovery) at the statutory rate of 43.12% (2000 – 44.62%)	(275,182)	(379,123)
Tax rate differential on foreign operations	27,042	40,646
Tax benefit of losses not recognized	248,140	338,477
	—	—

At December 31, 2001, the Company has the following approximate balances available to be claimed against future income for tax purposes:

	$
Undepreciated capital cost	368,000
Canadian exploration expenditures	228,000
Canadian development expenditures	500,000
Canadian oil and gas property expenditures	269,000
United Kingdom deductible expenditures	3,230,000
Foreign exploration and development expenditures	3,440,000
Undeducted share issue costs	103,000

In addition, as at December 31, 2001, the Company had the following approximate non-capital losses available to reduce future Canadian taxable income expiring as follows:

	$
2002	199,000
2003	1,000
2004	402,000
2006	129,000
2007	770,000
2008	904,000
Total	2,405,000

The Company also has subsidiary UK tax losses of approximately $686,000, which are not subject to expiry. The benefit of these losses has not been recognized in these financial statements.

Future income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts for income tax purposes. As at December 31, 2001 the Company has recognized a full valuation allowance against a future income tax asset arising from tax pools in excess of the net book value of capital assets, share issue costs and non-capital losses as follows:

	2001 $
Tax pools in excess of net book value of capital assets	214,038
Share issue costs	43,975
Domestic and foreign non-capital losses	1,230,591
	1,488,604
Less valuation allowance	(1,488,604)
Future tax asset	—

8. SHARE CAPITAL

(a) **Authorized**

Unlimited common shares without nominal or par value

(b) **Issued**

	Number of Shares	Amount $
Common shares		
Balance, December 31, 1999	8,502,336	7,807,728
Issued for cash	700,000	497,000
Exercise of stock options	10,000	5,600
Balance, December 31, 2000	9,212,336	8,310,328
Issued for cash	5,592,964	3,355,580
Exercise of stock options	176,667	74,800
Share issue costs	—	(128,662)
Balance, December 31, 2001	**14,981,967**	**11,612,046**

(c) **Stock Options**

The Company has established a stock option plan whereby the Company may grant options to its directors, officers and employees for up to 20% of the outstanding listed common shares with a maximum of 10% to insiders (on a non-diluted basis). The exercise price of each option equals the market price of the Company's shares on the date of the grant less any applicable discount approved by the Board of Directors and the Canadian Venture Exchange. The option's maximum term is five years, with the minimum vesting period to be 18 months. The stock options vest over the initial three years. No compensation expense is recognized for the plan when stock options are issued or exercised. Any consideration paid on exercise of stock options is credited to share capital.

The following is a continuity of stock options outstanding for which shares have been reserved:

	2001		2000	
	Options	Weighted Average Exercise Price $	Options	Weighted Average Exercise Price $
Opening balance	659,167	0.54	809,167	0.54
Granted	460,000	0.60	—	—
Exercised	(176,667)	(0.42)	(10,000)	(0.56)
Cancelled	(10,000)	—	(140,000)	(0.56)
Ending balance	932,500	0.59	659,167	0.54

The following table summarizes information about the stock options outstanding and exercisable at December 31, 2001:

Exercise Price	Number Outstanding December 31, 2001	Maturity Date	Number Exercisable December 31, 2001
$0.375	150,000	November 17, 2004	100,000
$0.40	7,500	January 12, 2004	5,000
$0.45	150,000	August 1, 2004	100,000
$0.60	460,000	January 23, 2006	—
$0.90	165,000	December 17, 2002	165,000
	932,500		370,000

(d) Warrants

In connection with private placements on January 17, 2001 and January 26, 2001, 2,037,184 and 103,956 warrants were issued, which give the holder the right to acquire one common share at $0.75 per common share and $0.90 per common share, respectively, exercisable at anytime within 24 months. No value has been ascribed to these warrants in these financial statements. As at December 31, 2001 all warrants remain outstanding.

9. COMMITMENTS

The Company is committed to an operating lease for office premises and storage facilities with remaining payments of $37,881 in 2002, the year of expiry.

10. FINANCIAL INSTRUMENTS

The fair market values of the Company's financial instruments, including cash and short term investments, accounts receivable, and accounts payable approximate their carrying values.

11. SEGMENTED INFORMATION

The Company's activities are conducted in four geographic segments: Canada, the United Kingdom, Romania and other international locations which include operations in France and Denmark.

December 31, 2001	Other International	Romania	United Kingdom	Canada and Corporate	Total
	$	$	$	$	$
Expenses	—	—	208,597	510,702	719,299
Other income	—	—	2,481	78,640	81,121
Net loss	—	—	206,116	432,062	638,178
Capital expenditures	135,489	1,534,739	680,152	1,418	2,351,798
Total assets	269,813	4,690,859	2,840,633	748,945	8,550,250

December 31, 2000	Other International	Romania	United Kingdom	Canada and Corporate	Total
	$	$	$	$	$
Expenses	—	—	272,070	606,124	878,194
Other income	—	—	2,052	26,473	28,525
Net loss	—	—	270,018	579,651	849,669
Capital expenditures	117,731	646,736	532,842	2,165	1,299,474
Total assets	134,324	3,152,062	1,990,633	598,969	5,875,988

12. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform to the current year's financial statement presentation.

Corporate Information

STERLING RESOURCES LTD.

Directors

Robert G. Welty
Chairman & Chief Executive Officer
Sterling Resources Ltd.

Stewart G. Gibson
President & Chief Operating Officer
Sterling Resources Ltd.
Managing Director
Sterling Resources (UK) Ltd.

Raj K. Agrawal
President
NRG Engineering Ltd.

J. Richard Harris
Independent Businessman

Philip C. Swift
Chief Executive Officer
ARC Financial Corporation

Officers

Robert G. Welty
Chairman & Chief Executive Officer

Stewart G. Gibson
President & Chief Operating Officer

Sherry L. Cremer
Treasurer & Corporate Secretary

Corporate Headquarters

Sterling Resources Ltd.
Suite 1306, 333 Seventh Avenue S.W.
Calgary, Alberta, Canada T2P 2Z1

Telephone: (403) 237-9256
Facsimile: (403) 215-9279

E-Mail: info@sterling-resources.com
Website: www.sterling-resources.com

Auditors

Ernst & Young LLP

Banker

The Royal Bank of Canada

Legal Counsel

Stikeman Elliott

Registrar and Transfer Agent

Inquiries regarding change of address, registered shareholdings, stock transfers or lost certificates should be directed to:

Computershare Trust Company of Canada
Suite 600, 530 Eighth Avenue S.W.
Calgary, Alberta, Canada T2P 3S8

Attn: Stock Transfer Department

Telephone: (403) 267-6800

E-Mail: caregistryinfo@computershare.com

Stock Exchange Listing

Canadian Venture Stock Exchange
Trading Symbol: **SLG**

STERLING RESOURCES (UK) LTD.

(wholly owned)

Directors

Robert G. Welty
Calgary, Canada

Stewart G. Gibson
Aboyne, Scotland

David Miller
London, United Kingdom

Officers

Robert G. Welty
Chairman

Stewart G. Gibson
Managing Director

Walter R. Roberts
Corporate Secretary

United Kingdom Office

Inneshewen House
Dess
Aboyne
Aberdeenshire
Scotland AB34 5BH

Telephone: 44-13398-84285
Facsimile: 44-13398-84092

Banker

Bank of Scotland

Sterling Resources Ltd.
Suite 1306, 333 Seventh Avenue S.W.
Calgary, Alberta, Canada T2P 2Z1